

November 19, 2007

Marlene H. Dortch, Secretary
Federal Communications Commission
Office of the Secretary
445 12th Street, SW
Washington, DC 20554

Re: Ex Parte Presentation
MB Docket No. 07-42

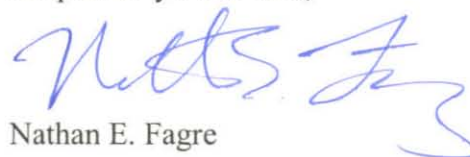
Dear Ms. Dortch:

Enclosed for filing in the above-referenced docket on behalf of ValueVision Media, Inc., the National Alliance for Media Arts and Culture, the Center for Creative Voices in Media, the United States Conference of Catholic Bishops, the United Church of Christ, Office of Communication, Inc., the National Hispanic Media Coalition, the Communications Workers of America, Free Press, U.S. PIRG, the Leased Access Producers Association, StogMedia, and Combonate Media Group is an affidavit executed by Dr. Mark R. Fratrik, Vice President of BIA Financial Network. Dr. Fratrik advances a reasonable proxy for the opportunity cost that would be incurred by a cable operator, assuming (notwithstanding the expanded channel capacity of digital cable systems) that its carriage of a leased access channel would require displacement of another channel on the operator's system.

As Dr. Fratrik explains, a direct measure of that opportunity cost would be the value that the cable operator realizes from the existing channel that is displaced. However, cable operators alone have access to that information and have elected not to provide the Commission with it. Dr. Fratrik's analysis demonstrates that a reasonable proxy for that value is the smallest amount that cable operators agree to *pay* to cable programmers for the right to carry their programming. He cites recent Kagan data reporting that a wide variety of cable networks are paid average license fees ranging from 1 to 4 cents per subscriber per month.

In accordance with Section 1.1206(b) of the Commission's Rules, 47 C.F.R. § 1.1206(b), this letter is being filed with your office.

Respectfully submitted,



Nathan E. Fagre

cc (w/encl.): Michelle Carey
Rick Chessen
Rudy Broche'
Amy Blankenship
Cristina Chou Pauze'
Monica Desai
Gregory Crawford

AFFIDAVIT OF DR. MARK R. FRATRIK

I, Dr. Mark R. Fratrik, being first duly sworn, depose and state as follows:

1. I am an economist currently serving as Vice President of BIA Financial Network, a provider of financial information and analysis and investment resources to the media, technology, telecommunications and related industries. As part of my duties at BIA Financial Network, I analyze the communications markets including radio, television, and cable industries. I am also an adjunct professor of economics at The Johns Hopkins University, specializing in the telecommunications and broadcast industries. I have worked as an economist specializing in economics and the media industry for over 27 years, working both in government at the Federal Trade Commission in the Bureau of Economics, and in the private sector at the National Association of Broadcasters, and the BIA Financial Network. A true and correct copy of my curriculum vitae is attached as Exhibit A to this Affidavit.

2. In MB Docket No. 07-42, the FCC is currently examining the rules for commercial leased access that it established in 1997. This reexamination was premised on concerns that independent programmers (i.e., those unaffiliated with cable operators) have still not found leased access to be a viable way of securing carriage on cable systems, notwithstanding the intention of Congress in the 1992 Cable Act to transform leased access into a genuine outlet for such independent programmers. Among the questions raised by the FCC in its Notice of Proposed Rulemaking in this proceeding are whether the terms of leased access are the same or similar to those that cable operators have with other programmers carried on their systems, whether the “average implicit fee” formula for leased access rates established by the

Commission ten years ago should be revisited, and how a different approach might “better serve Congress’ statutory objectives in a legally sustainable way.”

3. This affidavit addresses the economic rationale for establishing leased access rates through a mechanism that would better serve to measure the value of an analog or digital channel to the cable operator. The reason why the FCC needs to be involved in setting such a rate (apart from its legal obligation to do so) is important to restate. Local cable systems continue to control the distribution of video programs to a large majority of homes in the U.S. As of June 2005, the last measurement the FCC has made, 69.4% of all MVPD subscribers received video programming from a franchised cable operator.¹ In certain markets, however, this figure could be as high as 80% or even higher.² With this widespread coverage, local cable systems have significant market power that they have the ability and incentive to use in denying access to independent video programmers.

4. Ideally, in order not to adversely affect the local cable system while also encouraging the use of leased access channels, the FCC should examine the range of values cable systems realize from their existing channels in establishing an appropriate rate for leased access. The value to cable operators of any particular cable channel that they carry, referred to by economists as producer surplus, can be simply characterized as the sum of what they get in advertising revenue from that channel plus what the channel provides them, if anything, in subscriber retention revenues, minus what they pay the cable network for carriage of that channel. This analysis assumes, consistent with the FCC’s earlier decisions on leased access, that the attributable cost of

¹ *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB Docket No. 05-255, 21 FCC Rcd 2503 ¶ 8 (2006).

² The Honolulu, HI cable penetration was 89.0% as of July 2007, followed by Hartford-New Haven, CT penetration of 81.3% and Providence, RI-New Bedford, MA penetration of 81.2%. www.tvb.org/nav/build_frameset.asp

providing access to the channel to consumers is covered by the monthly fee they pay to the cable operator.

5. Unfortunately, there is no publicly available evidence of what cable systems presently earn from individual networks that they carry. However, one possible proxy for this value is what the cable system is willing to *pay* for the rights to carry these networks. NCTA has reported, for example, that the average license fee paid by cable operators for all basic cable networks is 15 cents per subscriber per month.³ While fees for some networks such as TBS and CNN range as high as 43 to 44 cents per subscriber per month, many others range from 1 to 4 cents per subscriber per month. These include B-Mania, VH1 Country, Fine Living, VH1 Soul, Anime, DIY, and Lifetime Real Women (all 4 cents); La Familia, MTV2 Blackbelt TV, and LOGO (all 3 cents); TV Guide, Bloomberg, AmericanLife TV, and Lime (all 2 cents); and Galavision, CNBC World, Si TV, Sportsman Channel, Great American Country, MTV Hits, and MTV Jams (all 1 cent).⁴

6. Use of this available information as a proxy for the values cable systems realize for these channels as a way of setting the price to be paid for leased access seems quite appropriate. First, the value to the cable system of carrying low-valued channels can be no less than the amount they realize from them, since they would not have elected to carry these networks if that were the case.

7. Second, the value to the cable system of carrying these channels is most likely not much more than that amount. These lower priced cable networks do not generate meaningful audiences, with many of them not receiving enough audience to be reportable in the local or

³ Written Statement and Comments of NCTA to the U.S. Copyright Office, Docket No. 2007-1 (July 2, 2007), pp. 12-13, citing Kagan Research, *Cable Program Investor*, Issue 112, pp. 7-9 (Mar. 30, 2007).

⁴ SNL Kagan, *Cable Program Investor*, Issue 114, pp. 3-4, (May 31, 2007) (2006 average license fees).

national audience estimate reports. Hence, they generate little additional advertising revenues for the local cable system other than as a way to place “run of system” spots.⁵ Nor, since they attract very little audience, do they add much to the ability of the local cable system to attract or retain subscribers. In other words, they generate very little, if any, producer surplus from being carried. Thus, the most accurate proxy for setting a value on the leased access channel capacity at issue in this proceeding would be the lowest price paid by the cable system operator for any channel that it elects not to carry due to the carriage of leased access channels.

8. An argument that might be offered against the use of such a proxy is that these low-priced cable networks are more valuable to local cable systems than the meager amounts that are spent on them. This argument is incorrect. As we see time and again, cable networks that are valuable to local cable systems continuously negotiate for higher prices, as shown by the recent negotiations for carriage of the Fox News Channels for substantially higher rates. As a result, if the lower priced cable networks currently being carried by cable systems became more valuable to them, then one would expect these networks to renegotiate their charges to cable operators over time. And even if one assumes that a few lower-priced networks result in greater producer surplus to cable systems at any given time, that will not be the case over time or over the entire range of lower-priced networks.

9. Another argument that might be offered against use of such a proxy is that it fails to account for subscriber losses resulting from carriage of untested and unknown leased access programming in lieu of existing cable networks. This argument also belies actual evidence

⁵ A paper written by David Waterman and Michael Z. Yan submitted to the FCC in MB Docket No. 04-207 provides strong evidence that lower viewed cable networks do not generate much in revenues as compared to other more viewed cable and over-the-air broadcast networks. That study shows that cable networks must reach a substantial number of potential viewers before they are able to generate significant revenues. D. Waterman & M. Yan, *Cable Advertising and the Future of Basic Cable Networking*, Journal of Broadcasting & Electronic Media, Fall 1999, at 645, attached to Joint Reply Comments of Altitude Sports & Entertainment and The Tennis Channel (August 13, 2004).

showing the opposite. First, the ever increasing capacity of cable systems with their digital channel tiers suggests that no substitution of channels may be required; the leased access channels will just be added to the lineup. Second, as discussed earlier, even if faced with limited channel capacity, the rational cable system will trade out its least popular channel, which is providing little if any producer surplus, to obtain capacity for a leased access channel. Such a substitution of unpopular for unknown programming cannot be expected to have any appreciable impact on the number of subscribers retained. Third, as the cable industry has suggested in other proceedings,⁶ consumers are indifferent to the loss of a few channels among the hundreds of channels they now receive, even assuming that there would be no interest in the newly offered leased access channels.

10. In the Notice of Proposed Rulemaking in this proceeding, the FCC has also noted the expanded availability of digital cable offerings, and asked how the digital transition may affect the rates for leased access. Of course, most cable programming is negotiated on the basis of a certain price per subscriber per month; thus, since digital tiers do not currently have as many subscribers, the overall payment by a leased access programmer should be less for placement on a digital tier than on the analog expanded basic tier. But even measured on a per subscriber basis, cable programmers view digital tiers as the equivalent of cable Siberia. The NFL Network, for example, has expressed in its comments in this proceeding strong disagreement with cable operators' placement of its service on a digital sports tier, available only to a limited number of subscribers today, in contrast to sports channels with which cable operators are affiliated, which are typically placed on tiers that have much wider distribution. This concern is understandable. Digital tiers currently are populated with a number of niche services that are not

⁶ Comments of NCTA at 5-6, 20 (July 15, 2004) (MB Docket No. 04-207); Response of NCTA to Staff Further Report on A La Carte at 19 (Mar. 15, 2006) (MB Docket No. 04-207).

widely viewed, and the channel surfing benefits to any programmer of being placed on such a tier are much lower. As the Waterman & Yan analysis described above also indicates, the value of a cable channel in terms of audience viewing turns to a significant degree not only on loyal viewers, but also on the ability to generate cumulative audience share from more episodic viewers. Thus, the per subscriber value of a digital channel should be less than for an analog expanded basic channel. This price distinction also accords with the lower bandwidth needed to make digital channels available.

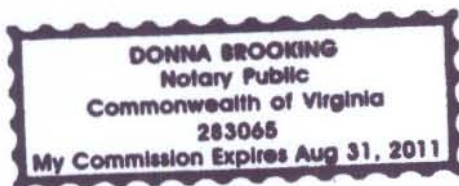
I declare under penalty of perjury under the laws of the Commonwealth of Virginia that the foregoing is true and correct to the best of my knowledge, information and belief.


Dr. Mark R. Fratrik
Vice President, BIA Financial Network

Sworn to and subscribed before me this 14th day of November, 2007.


Notary Public

My Commission expires: August 31, 2011



Curriculum Vitae

Mark R. Fratrik

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Education

Ph.D., 1981, Economics, Texas A&M University, College Station, TX
M.S., 1978, Economics, Texas A&M University, College Station, TX
B.A., 1976, Mathematics and Economics (honors), State University of New York at Binghamton

Professional experience

2001 – Present

BIA Financial Network

Vice President

- Consulting in litigation and tax-related cases
- Developing of new broadcasting and related industry research offerings
- Speaking at industry forums

Fall 2002 – Present

The Johns Hopkins University

Adjunct Professor, *The Political Economy of Mass Communications*

1985 – 2000

National Association of Broadcasters

Vice President/Economist 1991 – 2000

- Supervised the Research and Planning Department.
- Conducted primary research about the broadcasting and related industries, used for testimony before the Congress and in filings at the FCC and other governmental agencies.
- Conducted research and studies included in publications and reports distributed by NAB.
- Presented results of primary research and other analyses at industry forums.

Director of Financial and Economic Research 1985 -- 1991

- Supervised the collection and dissemination of the annual industries financial reports

Curriculum Vitae - Mark R. Fratrik

1980 – 1985

Federal Trade Commission
Bureau of Economics
Staff Economist

- Conducted analysis of proposed mergers and other arrangements.
- Conducted analyses of industry practices to evaluate economic impact.
- Participated in litigation support in several antitrust cases.

Professional activities

Broadcast & Cable Financial Management Association – Board Member 2001-2004
American Economic Association – member
Southern Economic Association – member
Journal of Media Economics – reviewer
Journal of Broadcasting and Electronic Media - reviewer

Articles

“Loosen Up, Already,” *Broadcasting & Cable*, April 18, 2005, p. 37.

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Radio Industry Revenue: Radio Revenues: Is the Bloom Back?, 2002, BIA Financial Network

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RadiOutlook: Forces Shaping the Radio Industry (with John Abel & Richard Ducey), April 1988, National Association of Broadcasters.

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The Small Market Television Manager's Guide (editor), 1987, National Association of Broadcasters.

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Policy Research

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CBS Broadcasting, Inc., et. al. vs. Echostar Communications Corporation, et. al., U.S. District court for the Southern District of Florida, deposed on April 1, 2003

Curriculum Vitae - Mark R. Fratrik

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Salem Media of Virginia, Inc. v. WAVA Limited Partnerships et. al., deposition pending.